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SUBJECT: VODACOM COURT DECISION PROVIDES TEMPORARY REASSURANCE TO
FOREIGN INVESTORS

REF:
¶A. 09 PRETORIA 981
¶B. 09 JOHANNESBURG 82
¶C. 09 PRETORIA 249
¶D. 09 PRETORIA 473

This cable contains company proprietary information.

¶1. (SBU) Summary. Vodacom listed its shares on the Johannesburg Stock Exchange (JSE) on May 18 after legal actions by the Congress of South African Trade Unions (COSATU) and ICT regulator the Independent Communications Authority of South Africa (ICASA) failed to stop the unbundling of state-controlled, fixed-line operator Telkom and mobile operator Vodacom. The dissolution had the support of industry and the outgoing administration because it would provide a large boost in foreign direct investment, improve sector competitiveness, and allow Telkom and Vodacom to pursue independent investment strategies in Africa. Last-minute COSATU activism almost derailed the process. Continued labor actions combined with ICASA's last-minute decision to support COSATU have heightened investor fears regarding the South African investment climate. Foreign and local market entrants have had to depend on a series of court decisions to uphold legislation and initiatives intended to increase ICT market liberalization. There is potential for ICT market growth in South Africa, especially with the introduction of additional broad-band capacity beginning as early as July 2009. However, the slow pace of implementation of liberalization policies combined with continued labor activism could deter foreign investment and competition, which is required to mitigate high ICT costs stemming from Telkom's historic monopoly control of the country's ICT infrastructure. Foreign investors were closely watching the incoming Zuma administration for signals of economic policy shifts towards the left and took COSATU's interventions as a negative sign for future investment potential. The new administration will have to continue to reassure investors that COSATU will not be determining national economic policy if it hopes to continue to attract the foreign investment needed to maintain high levels of economic growth and employment. End Summary.

COURT DECISION ALLOWS VODACOM
TO PROCEED WITH JSE LISTING

¶2. (U) Mobile-operator Vodacom listed its shares on the Johannesburg Stock Exchange (JSE) on May 18 after legal actions by the Congress of South African Trade Unions (COSATU) and ICT regulator the Independent Communications Authority of South Africa (ICASA) failed to stop the unbundling of Telkom and Vodacom. The listing is part of a deal that involves state-controlled, fixed-line operator Telkom selling a 15 percent stake in Vodacom to UK-based, joint-owner Vodafone. The court decision allows Vodafone to increase its ownership in Vodacom from 50 to 65 percent and to expand its emerging-market footprint. Telkom is spinning-off the remaining 35

percent to its shareholders (except for U.S. stakeholders, who will receive cash).The South African Government (Telkom's top shareholder) has pledged to hold 10 percent of Vodacom for at least a year.

¶3. (SBU) The dissolution had the approval of the outgoing administration because it would provide a large boost in foreign direct investment. Telkom's relationship with mobile operator Vodacom had been difficult and under the partnership agreement Telkom was restricted from offering mobile services. Vodacom also lost out on lucrative mobile deals in Africa because the agreement Qlost out on lucrative mobile deals in Africa because the agreement prevented it from operating in some parts of Africa where Vodafone was present. The split is expected to allow both to pursue independent investment strategies that would improve consumer product offerings and improve sector competitiveness. Proceeds from the Vodacom sale would allow Telkom to pursue its strategy of further expansion into sub-Saharan Africa. Finalization of operational details for Telkom's recently announced partnership with AT&T had been delayed partially due to Telkom's inability to complete the sale of Vodacom shares (Reftel A). The new partnership with AT&T would allow Telkom to leverage AT&T's network (which has a 97 percent global reach) and meet the infrastructure requirements Telkom has agreed to provide FIFA for the 2010 World Cup.

COSATU AND ICASA INTERVENTIONS
ALMOST DERAILED DEAL

¶4. (SBU) Last-minute labor activism almost derailed the long-awaited dissolution of the Telkom-Vodacom partnership, which permitted the independent Vodacom JSE listing. COSATU sought legal action against

Telkom, the Minister of Communications, Vodafone, and Vodacom to impede the pending sale (Reftel B). In a move that surprised industry analysts, ICASA reversed its prior decision to support the unbundling and joined the legal case in solidarity with COSATU. COSATU expressed concern that the UK-based Vodafone group would use the global economic crisis as an excuse to cut jobs as part of its justification for pursuing legal action. Vodacom announced on May 19 that it would not eliminate jobs as a result of the dissolution.

¶5. (U) Local Economist Peter Montalto said there were political rifts behind the scenes that led to ICASA's change of heart. The outgoing government, National Competition Tribunal, and ICASA all approved the transaction in February and the regulator had months to raise objections. Montalto speculated that COSATU-affiliated ministers in the new administration might have had "undue influence on the industry regulator, which buckled under pressure and joined the bid to stop the listing so it could stage public hearings on the transaction."

6 (SBU) ICASA announced that it would not challenge the May 18 court ruling in favor of the dissolution and would not pursue public hearings. However, COSATU officials told Labor Officer the union would not back down despite the court ruling. COSATU is now calling for a boycott of Vodacom and has vowed to continue with an existing application for a full legal review of Telkom's unbundling of Vodacom. The boycott is seen as an empty threat and is not expected to negatively impact Vodacom's bottom-line since MTN is currently the only main rival providing mobile services in South Africa. MTN's mobile service rates are higher than Vodacom's and the third mobile-operator, Cell C, utilizes Vodacom's network.

LABOR INTERVENTIONS SHAKE
INVESTOR CONFIDENCE

¶7. (U) Continued COSATU actions combined with ICASA's decision to support COSATU have heightened investor fears regarding the South African investment climate. The South African currency declined by

three percent on May 15, when COSATU's legal actions threatened the deal. Vodafone had already brought R20.5 billion ($2.4 billion) into the country to fund the deal, so blocking it would have further hurt the currency. Annulment of the deal combined with the rand's decline (blamed largely on COSATU) would have inflicted a national foreign exchange loss of R500 million ($59 million). The rand recovered by 1.2 percent on May 18 after the court ruled in favor of the Vodacom deal.

¶8. (U) The local press reports that foreign investors have called on President Zuma to clarify South Africa's stance on foreign investment, warning that union activism could herald the start of a new investor-deterring trend. Investors are demanding for the new administration to spell out its economic policies more clearly, particularly since COSATU is going to continue with legal challenges against the Vodacom deal despite the May 18 court ruling. Analysts warned that a South African decision to block majority foreign ownership of Vodacom could also harm South African companies such as Telkom and MTN, who were trying to expand on the continent, if other African countries decided to adopt similar policies.

COURTS CONTINUE TO UPHOLD
MARKET LIBERALIZATION

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¶9. (SBU) Foreign and local market entrants have depended on a series of court decisions to uphold legislation and initiatives intended to increase ICT market liberalization. Analysts said "the failure of COSATU's bid to halt the listing was welcome evidence of judicial independence that will help to salvage South Africa's reputation among global investors." Similarly, former Minister of Communications Matsepe-Caseburri (Reftel C) and her Director General Lyndall Shope-Mafole thwarted implementation of the 2005 Electronic Communications Act (ECA) and ICASA independence until the courts interceded on behalf of market liberalization.

¶10. (U) Matsepe-Caseburri publicly advocated a policy of "managed liberalization" during her tenure and personally intervened to block ICASA from converting value-added network service (VANS) licenses into individual electronic communications network service (I-ECNS) licenses required to develop national networks that would compete with Telkom (Reftel C). Her interventions delayed the license conversion process by three-years and the process was only completed after a Pretoria high court decision finally forced ICASA to

complete licensing in January 2009.

NEW APPOINTMENTS
PUZZLE INDUSTRY

¶11. (SBU) Industry analysts had high hopes for new leadership at the Ministry of Communications after the death of Matsepe-Cassaburri in March 2009. Her death and the ousting of Shope-Mafole for supporting the new opposition COPE Party had left a leadership vacuum at the Ministry of Communications that industry analysts had hoped would have been filled with someone with technical expertise in the sector. However, industry analysts were perplexed by the appointment of Siphiwe Nyanda, a former military general with no ICT background, as the new Minister of Communications. Nyanda was chief of staff of the African National Congress' (ANC) military wing during the anti-apartheid struggle and then held senior armed forces posts after the ANC won power in 1994.

¶12. (SBU) Industry analysts speculate that Nyanda's lack of experience in the sector could mean that he would take "a cautious approach, steering clear of bold steps" needed to improve competitiveness. According to press reports, new Director General Dina Pule (a left-leaning activist) may become a vocal second in command. "She has a history of being quite fearless in her criticism of mismanagement and corruption, which may make life difficult for Telkom's underperforming management."

COMMENT

¶13. (SBU) There is potential for ICT market growth in South Africa, especially with the introduction of additional under-sea, fiber-optic, broad-band capacity and new competitive partnership agreements with international companies such as AT&T and Tata Corporation. However, the slow pace of ECA implementation and COSATU activism could deter foreign investment and competition, which is needed to offset high ICT costs stemming from Telkom's historic monopoly control of fixed-line, mobile, and satellite infrastructure. ICASA's recent change of heart to rescind its earlier support for the Vodacom sale indicates that the regulator's independence is still hampered by political considerations despite leadership change at the Ministry of Communications. Recent market liberalization efforts have only proceeded as a result of legal decisions by the independent courts.

¶14. (SBU) Foreign investors were closely watching the incoming Zuma administration for signals of economic policy shifts towards the left and took COSATU's interventions as a negative sign for future investment. COSATU believes its political clout has increased because of its support for Zuma's candidacy and its recent success in getting the South African Airways (SAA) CEO ousted for irregularities in tender contracting at the state-owned airline (Reftel D). The new administration will have to continue to reassure investors that COSATU will not be determining national economic policy if it hopes to continue to attract the foreign investment needed to maintain high levels of economic growth and employment. End Comment.

LA LIME